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PAGE 01 OECD P 29003 01 OF 04 011858Z

73

ACTION EUR-12

INFO OCT-01 EA-07 ISO-00 AID-05 CEA-01 CIAE-00 COME-00

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STR-04 AGR-05 AGRE-00 FEA-01 INT-05 EURE-00 /099 W
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P R 011835Z OCT 76

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PASS CEA, TREASURY, FRB

MANILA PASS USDEL TO IMF/IBRD ANNUAL MEETING

E.O.11652: N/A

TAGS: ECON, OECD

SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC)

SPECIAL MEETING: CURRENT IMPRESSIONS OF SHORT-TERM

ECONOMIC PROSPECTS

1. SUMMARY: SPECIAL EDRC ON SEPTEMBER 30 DEVOTED LARGELY TO OECD SECRETARIAT'S PRESENTATION OF ITS CURRENT IMPRESSIONS OF SHORT-TERM PROSPECTS. THIS ASSESSMENT WAS OF PRELIMINARY NATURE, SINCE SECRETARIAT ONLY BEGINNING ITS DETAILED ANALYSIS AND FORECASTING ROUND WHICH WILL CULMINATE IN NOVEMBER EPC AND PUBLICATION OF DECEMBER "ECONOMIC OUTLOOK." ON BASIS MOST RECENT DATA, SECRETARIAT REVISED DOWNWARD ITS ESTIMATES OF FIRST HALF 1976 BIG 7 AND OECD AREA GNP GROWTH FROM FIGURES CONTAINED IN JULY "ECONOMIC OUTLOOK" (SEE TABLE 1, PARA 6).

SECRETARIAT DID NOT PRESENT SPECIFIC FORECAST FOR SECOND HALF OF 1976, BUT STATED THAT PRESENT INDICATIONS

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PAGE 02 OECD P 29003 01 OF 04 011858Z

SUGGESTED OECD AREA REAL GNP GROWTH MIGHT BE LOWERED

TO 3.75 PERCENT FROM 4.75 PERCENT FORECAST CONTAINED IN OUTLOOK. SECRETARIAT EXPLAINED THAT TEMPORARY FACTORS (E.G., CESSATION OF INVENTORY DECUMULATION, FISCAL STIMULATORY MEASURES, CATCH-UP PURCHASES BY CONSUMERS), WHICH HAD GIVEN BOOST TO EARLY PHASE OF RECOVERY, HAD NOW SPENT THEMSELVES AND THAT MORE BASIC WEAKNESSES (SLOW GROWTH IN REAL DISPOSABLE INCOME, FLAGGING INVESTMENT, ETC.) WERE EMERGING AS MORE INFLUENTIAL FACTORS. SECRETARIAT EMPHASIZED THAT SLACKENING OF OECD GROWTH PERFORMANCE PRIMARILY CONFINED TO EUROPE, WHERE WEAKNESS IN FIXED INVESTMENT SPENDING MOST PRONOUNCED. GROWTH OF OECD TRADE ALSO LESS THAN FORECAST IN JULY OUTLOOK AND REFLECTIVE OF SLOWER GROWTH IN OVERALL DEMAND. ON PRICE/WAGE FRONT, SECRETARIAT FELT RESULTS IN SECOND HALF OF 1976 MIGHT ON OVERALL OECD BASIS BE SOMEWHAT LOWER THAN FORECASTED. HOWEVER, SECRETARIAT INDICATED THAT COUNTRIES WITH RELATIVELY LOW INFLATION RATES LIKELY TO DO EVEN BETTER THAN EXPECTED PREVIOUSLY, WHILE MANY POOR PERFORMERS WOULD PROBABLY NOT IMPROVE. IMPLICATION IS THAT INTRA-OECD PRICE AND GROWTH PERFORMANCE COULD DIVERGE FURTHER IN SECOND HALF OF THE YEAR. SECRETARIAT DID NOT HAZARD GUESS ON 1977 OUTLOOK. SECRETARIAT ALSO GAVE OVERVIEW OF DEVELOPMENTS IN EACH OF BIG 7 COUNTRIES, BUT PRESENTATIONS WERE GENERAL AND ADDED LITTLE TO INFORMATION CONTAINED IN GENERAL ASSESSMENT. END SUMMARY.

2. SHORT-TERM OUTLOOK; DOMESTIC DEMAND: ON BASIS MOST RECENT DATA, SECRETARIAT NOW ESTIMATES THAT MAJOR SEVEN OECD COUNTRIES' ANNUAL RATE OF GNP GROWTH WAS 6.7 PERCENT IN FIRST HALF OF 1976 COMPARED WITH 7.25 PERCENT ESTIMATE CONTAINED IN JULY ECONOMIC OUTLOOK. FOR ENTIRE OECD AREA, DOWNWARD REVISION WAS FROM 6.5 PERCENT TO 6.2 PERCENT. SECRETARIAT EXPLAINED THAT FACTORS DRIVING RECOVERY IN ITS EARLY PHASE WERE BY NATURE TEMPORARY. THESE INCLUDED: (1) CESSATION OF INVENTORY LIQUIDATION; (2) SHARP CATCH-UP INCREASE IN CONSUMER DURABLE PURCHASES FINANCED BY REDUCTION IN SAVINGS; (3) ONE-SHOT INJECTION OF POLICY STIMULUS BY SEVERAL MAJOR COUNTRIES. SECRETARIAT ARGUED THAT STIMULATORY EFFECT OF THESE IMPULSES HAS TAPERED OFF, ALLOWING MORE BASIC WEAKNESSES LIMITED OFFICIAL USE

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PAGE 03 OECD P 29003 01 OF 04 011858Z

TO EMERGE, WITH A RESULTANT SLOWDOWN IN GROWTH. IN SECRETARIAT VIEW, MAJOR FACTORS RETARDING GROWTH ARE: (A) SLOW GROWTH IN REAL DISPOSABLE INCOME. GOVERNMENTS MAKING EFFORTS TO REDUCE INCREASES IN NOMINAL INCOMES AND SINCE FAVORABLE PRICE EFFECTS OF SLOWER NOMINAL INCOME GROWTH WOULD OCCUR WITH A LAG, REAL DISPOSABLE INCOME GROWTH IS CURRENTLY BEING SQUEEZED; (B) EXPECTED ACCELERATION OF REAL FIXED INVESTMENT SPENDING HAS NOT

YET MATERIALIZED DESPITE SOME SHIFT IN INCOME DISTRIBUTION TOWARD PROFITS. SECRETARIAT NOTED THAT STAGNATION OF FIXED INVESTMENT SPENDING IS PRIMARILY CONFINED TO EUROPE, WHERE SUBSTANTIAL EXCESS CAPACITY EXISTS AND WHERE COMPANIES' BALANCE SHEETS ARE IN BAD SHAPE. SECRETARIAT COMMENTED THAT IN JAPAN AND U.S. INVESTMENT SPENDING IS STRONGER, BUT IS NOT PROCEEDING AS RAPIDLY

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PAGE 01 OECD P 29003 02 OF 04 011857Z

73

ACTION EUR-12

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P R 011835Z OCT 76

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LIMITED OFFICIAL USE SECTION 02 OF 04 OECD PARIS 29003

AS SECRETARIAT HAD HOPED. SECRETARIAT ADDED THAT INVESTOR CONFIDENCE APPEARS TO BE MUCH LOWER IN EUROPE THAN IN U.S. AND JAPAN; (C) DEMAND MANAGEMENT POLICIES HAVE MOVED TOWARD RESTRICTION IN MOST MAJOR COUNTRIES, PARTICULARLY IN FRANCE (SECRETARIAT OUTLINED BARRE PLAN, BUT HAS NOT YET COMPLETED QUANTITATIVE ESTIMATION OF PLAN'S MACRO-ECONOMIC IMPACT).

3. TRADE AND CURRENT BALANCE: SECRETARIAT NOTED THAT OECD IMPORT AND EXPORT VOLUMES GENERALLY FOLLOWED

PATTERN OF OECD GNP GROWTH IN FIRST HALF OF 1976. BOTH IMPORT AND EXPORT VOLUMES GREW MORE QUICKLY THAN EXPECTED IN FIRST HALF OF 1976 BECAUSE OF SLOWDOWN OF STOCK DECUMULATION (AND SOME STOCK ACCUMULATION) DURING THIS PERIOD. HOWEVER, SECRETARIAT ADDED THAT SIGNIFICANT DECELERATION IN GROWTH OF TRADE WAS ALREADY IN EVIDENCE IN SECOND QUARTER OF 1976, AND STRESSED THAT BETWEEN APRIL AND JULY OF THIS YEAR, GROWTH OF INTRA-OECD EXPORTS OF LARGE COUNTRIES VIRTUALLY STAGNATED. LIMITED OFFICIAL USE

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PAGE 02 OECD P 29003 02 OF 04 011857Z

SECRETARIAT SUGGESTED THAT STAGNATION OF LARGE COUNTRY EXPORTS BODED ILL FOR SUSTAINABILITY OF RECOVERY IN 1977, BUT DREW NO FIRM CONCLUSIONS FROM THIS DEVELOPMENT. SECRETARIAT NOW PUTS OECD AREA FIRST HALF 1976 CURRENT ACCOUNT DEFICIT AT \$7.8 BILLION COMPARED WITH JULY OUTLOOK ESTIMATE OF \$10 BILLION DEFICIT. SECRETARIAT MADE OBVIOUS POINT THAT EVOLUTION OF OECD CURRENT ACCOUNT IN 1977 WOULD DEPEND IMPORTANTLY ON SIZE OF ANY OIL PRICES INCREASE AT END 1976. (SEE PARA 5)

4. COSTS AND PRICES: IN CONTRAST TO ITS LESS-THAN-SANGUINE VIEW OF GROWTH OUTLOOK, SECRETARIAT FELT THAT PRICE INCREASES IN SECOND HALF 1976 MIGHT BE SOMEWHAT LESS THAN FORESEEN IN JULY. UNDERLYING SECRETARIAT'S PRICE ASSESSMENT WERE FOLLOWING DEVELOPMENTS: (A) TREND AND PATTERN OF DEMAND. RAPID GNP GROWTH WITH STRONG RESTOCKING COMPONENT IN FIRST QUARTER OF 1976 INDUCED STRONG RISE IN PRICES OF INDUSTRIAL RAW MATERIALS. IN CONTRAST, END OF STOCK CYCLE AND SLACKENING OF OVERALL DEMAND HAS ENTRAINED REVERSE MOVEMENT OF RAW MATERIALS PRICES. SECRETARIAT NOTED THAT INDUSTRIAL RAW MATERIALS PRICES HAVE DROPPED BY 15 PERCENT SINCE JULY PEAK; (B) ABUNDANT WHEAT AND CORN CROPS IN U.S. AND USSR OFFSET POOR HARVESTS IN WESTERN EUROPE. IN ADDITION, SHORT-TERM EFFECT OF DROUGHT HAS BEEN TEMPORARY DROP IN MEAT, FRUIT AND VEGETABLE PRICES IN EUROPE. HOWEVER, TEMPORARY PRICE RESPITE SHOULD END FOR THESE PRODUCTS DURING 1977; (C) WAGE SETTLEMENTS MODERATE IN SOME MAJOR COUNTRIES.

5. BIGGEST UNCERTAINTY CONCERNING PRICE OUTLOOK FOR 1977 IS PROSPECTIVE EVOLUTION OF OIL PRICES. SECRETARIAT STATED VIEW THAT OIL MARKET HAS FIRMED UP CONSIDERABLY DURING THE SUMMER, EFFECTIVE PRICES ARE UP (PERHAPS BY 5-6 PERCENT IN PAST 12 MONTHS), PRODUCER STOCKS ARE REDUCED AND CONSUMER STOCKS CONTINUE TO GROW (PARTLY IN ANTICIPATION OF OPEC PRICE INCREASE IN DECEMBER). NEVERTHELESS, SECRETARIAT JUDGMENT IS THAT GIVEN DEMAND PROSPECTS, UNLESS WINTER COLDER THAN AVERAGE, OPEC WOULD

HAVE TO REDUCE PRODUCTION FROM CURRENT LEVELS TO MAKE
STICK AN OIL PRICE INCREASE IN EXCESS OF 15-10 PERCENT.
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PAGE 03 OECD P 29003 02 OF 04 011857Z

6. TABLE 1

GROWTH OF REAL GDP IN THE OECD AREA (B)

	FROM PREVIOUS HALF-YEAR (ANNUAL RATES) 1976 I	
	MOST RECENT DATA	EO 19 (A)
CANADA (C)	5.5	6
U.S. (C)	6.5	7
JAPAN (C)	8.2	7.75
FRANCE	7.3	9.25
GERMANY (C)	7.1	8
ITALY	7.5	4.25
U.K.	3.6	4.75
7 MAJOR COUNTRIES	6.7	7.25

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PAGE 01 OECD P 29003 03 OF 04 011901Z

73
ACTION EUR-12

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EB-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 USIA-06

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P R 011835Z OCT 76
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LIMITED OFFICIAL USE SECTION 03 OF 04 OECD PARIS 29003

TOTAL OECD 6.2 6.5

(A) JULY 1976 ECONOMIC OUTLOOK
 (B) 1975 GNP/GDP WEIGHTS AND EXCHANGE RATES
 (C) GNP

TABLE 2

OECD TRADE IN 1976

(PERCENTAGE CHANGES IN VOLUME, AT ANNUAL RATES)

	ACTUAL			FORECAST EO 19 (A)		
	FIRST	FIRST	SECOND	FIRST	SECOND	
	Q1	Q2	HALF	HALF	HALF	
IMPORTS						

CANADA	23.5	8	15.5	11.25	9.25	
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U.S.	41	9.5	26.5	29.25	10.25	
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JAPAN	-1	.5	1.5	3	20.25	
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PAGE 02 OECD P 29003 03 OF 04 011901Z

FRANCE	26.5	20	27	18	14.25	
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GERMANY	28	11.5	21	20.5	9	
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ITALY	-9	-10	5.5	1	-5	
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U.K.	-6	37	6.5	6	12	
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TOTAL,BIG 7	17.5	11	16.5	15.5	10.5	
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TOTAL OECD	14.5	10.5	15.5	14	9	
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EXPORTS

CANADA	42.5	7	22	14.5	7	
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U.S.	-17.5	25	-L.5	-4.5	9	
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JAPAN	85.5	1.5	49	49.5	5.75	
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FRANCE	25.5	27	21	15.5	10.5	
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GERMANY	26	8	19.5	17.75	7	
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ITALY	-.5	-4.5	3	7	11	
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U.K.	11	14.5	16.5	18	8	
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TOTAL,BIG 7	17	13	16.5	15	8	
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TOTAL OECD 13.5 11.5 14 13 8.5

(A) JULY 1976 ECONOMIC OUTLOOK

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PAGE 01 OECD P 29003 04 OF 04 011900Z

73

ACTION EUR-12

INFO OCT-01 EA-07 ISO-00 AID-05 CEA-01 CIAE-00 COME-00

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STR-04 AGR-05 AGRE-00 FEA-01 INT-05 EURE-00 /099 W

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P R 011835Z OCT 76

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LIMITED OFFICIAL USE SECTION 04 OF 04 OECD PARIS 29003

TABLE 3

CURRENT BALANCES

1976 I

1976 (\$ BILLION)

FORECAST EO19(A) ACTUAL

CANADA	-2.5	-2.5
U.S.	-1.0	0.6
JAPAN	2.75	3.2
FRANCE	-1.0	-1.9
GERMANY	1.25	2.3

ITALY	-1.75	-1.5
U.K.	-1.0	-1.1
TOTAL, BIG 7	-3.25	-1.1
TOTAL, OECD	-10	-7.8
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PAGE 02 OECD P 29003 04 OF 04 011900Z

(A) JULY 1976 ECONOMIC OUTLOOK
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